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In the Supreme Court of the United States

OCTOBER TERM, 1997

IVAN D. JONES, JR., PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

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15 pp

QUESTION PRESENTED

Whether a disciplinary action against petitioner by the National Association of Securities Dealers, Inc. (NASD) for certain conduct precludes the Securities and Exchange Commission (SEC) from bringing an administrative action against petitioner for securities law violations arising out of the same conduct.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. B1-B27) is reported at 115 F.3d 1173. The opinion of the Securities and Exchange Commission (Pet. App. A1-A24) is not yet reported.

JURISDICTION

The judgment of the court of appeals was entered on June 16, 1997. A petition for rehearing was denied on August 12, 1997. Pet. App. B28-B29. The petition for a writ of certiorari was filed on November 10, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The Securities Exchange Act of 1934 (Exchange Act) and the Investment Advisers Act of 1940 (Advisers Act) grant the Securities and Exchange Commission (SEC) broad authority to institute disciplinary proceedings against broker-dealers, investment advisers, and persons associated with those market professionals. 15 U.S.C. 78o(b)(4) and (6), 80b-3(e) and (f). In 1938, Congress enacted the Securities Exchange Act Amendments of 1938 (known as the Maloney Act) to allow for the registration with the Commission of "self-regulatory" associations of brokers and dealers. 15 U.S.C. 78o-3, 78s. The National Association of Securities Dealers, Inc. (NASD), "which is a private, nonprofit corporation organized under the laws of Delaware," is the only association registered under the Maloney Act. Pet. App. B13; see also *United States* v. *National Ass'n of Sec. Dealers, Inc.*, 422 U.S. 694, 700-701 n.6 (1975).

As a registered national securities association, the NASD has the authority to regulate its members to ensure compliance with certain of the federal securities laws and with the NASD's own rules, which must be designed, among other things, to "promote just and equitable principles of trade." 15 U.S.C. 78o-3(a) and (b). The NASD may bring disciplinary proceedings against its members and persons associated with members for certain violations of the securities laws. 15 U.S.C. 78o-3(b)(7) and (h). A final disciplinary sanction order by the NASD is reviewable by the SEC, which may affirm, modify, or set aside the sanction imposed by the NASD, or remand for further proceedings. 15 U.S.C. 78s(d)(2), (e)(1), and (e)(2).

2. Petitioner was an officer and director of Akers and Jones Securities, Inc., a securities brokerage firm. Beginning in 1989, Akers and Jones Securities underwrote an offering of common stock by Sidbury Land Company. Contrary to the representations in the offering circular, petitioner failed to deposit subscribers' funds in a bank-controlled escrow account; prematurely withdrew subscribers' funds before the closing date of the offering; used subscribers' funds for purposes not specified in the offering circular; failed to return investor funds or distribute a revised circular when conditions specified in the offering were not met; and improperly offered prospective buyers a guarantee against loss. Pet. App. B3-B6.[1]

Also beginning in 1989, Akers and Jones Securities began operating with net capital deficiencies and failing to report those deficiencies, in violation of the securities laws. Pet. App. B7-B8. The firm also failed to maintain blotters of securities transactions and ledgers reflecting the firm's financial condition, and failed to file certain quarterly and annual financial reports, as well as other reports, with the SEC. Pet. App. B7-B8.

The NASD subsequently brought disciplinary proceedings against petitioner and his brokerage firm for fraud and for failing to maintain adequate net capital

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[1] Petitioner also failed to comply with the terms of an offering of securities in the form of partnership interests in One Virginia Partners, which petitioner marketed through his investment adviser firm, Investment/Timing Systems. As with the Sidbury offering, petitioner failed to deposit the offering proceeds in an escrow account as required by the offering materials. He also disbursed partners' funds for purposes not specified in the partnership agreement without obtaining the partners' consent. Pet. App. B6.

and adequate books and records. In 1992, under a settlement with the NASD, petitioner agreed to a censure, a suspension from association with any NASD member for three business days, a requirement that he requalify as a securities industry professional, and a $22,500 fine. Pet. App. B8.

In 1993, the SEC instituted administrative proceedings against petitioner based on the same conduct that was the subject of the NASD proceeding. After a hearing, an administrative law judge (ALJ) found that petitioner engaged in violations of antifraud, net capital, books and records, and reporting provisions of the securities laws. The ALJ suspended petitioner from association with any broker-dealer or investment adviser for one year and barred him from thereafter associating in a proprietary, supervisory, or managerial capacity, with the right to reapply after 18 months. The ALJ also censured petitioner and entered an order directing him to cease and desist from future violations. Pet. App. B9. The SEC sustained the ALJ's findings and the sanctions imposed. *Id.* at A1-A24.

3. The court of appeals affirmed. Pet. App. B1-B27. It rejected petitioner's argument that, under principles of res judicata, the NASD's disciplinary proceeding precluded the Commission's administrative proceeding. *Id.* at B10-B19. The court found that petitioner did not establish an identity of cause of action and parties between the two actions. The court explained (*id.* at B12) that "the NASD's enforcement action is not the same cause of action as the SEC's own later enforcement action," because the SEC's enforcement authority is broader.

The court further reasoned that "[t]he SEC was not a party to the NASD proceeding," Pet. App. B16,

or in privity with a party, *id.* at B17. The court explained that its conclusion was not altered by the fact that the Maloney Act, 15 U.S.C. 78s(d), authorizes the SEC to review final NASD disciplinary orders:

> [The SEC's] role, if any, was as potential reviewer of the NASD proceeding. But in this case, the SEC did not review the NASD's sanction. Even had it exercised the right of review, however, as reviewer, the SEC does not become a party; its role is an adjudicatory one.

Pet. App. B16-B17.

The court similarly rejected petitioner's argument that Congress intended that the NASD's disciplinary authority over its members under the Maloney Act would preclude SEC enforcement authority to sanction the same conduct. Pet. App. B19-B22. The court reasoned that petitioner could not point to "any statutory provision, statutory interpretation, or legislative history that makes NASD-initiated discipline and the SEC-initiated discipline mutually exclusive." *Id.* at B20. The court further explained that although the SEC retains substantial oversight authority over NASD disciplinary proceedings, the SEC "also has separate and distinct authority to execute the securities law when it determines that the public interest requires it." *Id.* at B21-B22.[2]

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[2] The court also held (Pet. App. B22-B24) that the SEC's sanctions did not violate the Double Jeopardy Clause. Petitioner does not challenge that ruling in this Court.

ARGUMENT

Petitioner renews his contention (Pet. 4-11) that the NASD's exercise of authority to discipline its members under the Maloney Act precludes subsequent SEC proceedings based on the same conduct. We are aware of no decision, however, that has accepted that argument. In any event, the court of appeals properly rejected it, finding "no statutory, regulatory, or historical reference to support [petitioner's] argument that NASD discipline of its members was intended to preclude * * * disciplinary action by the SEC itself against a securities professional." Pet. App. B14. Accordingly, the court of appeals correctly held that the SEC's enforcement action in this case was not barred by the earlier proceeding by the NASD.

1. Petitioner contends (Pet. 4-8) that the SEC's proceeding circumvents the terms of the Maloney Act that grant the SEC the power to affirm, modify, or set aside a NASD sanction, 15 U.S.C. 78s(e)(1), but not to increase it. The SEC's role as adjudicator over NASD proceedings, however, does not limit the SEC's separate statutory authority to impose sanctions when it functions as a prosecutor in its own proceeding. As the court of appeals explained, "the NASD's interest is that of a professional association charged with regulating itself, and the interest of the SEC is that of a policing agency that reviews NASD action and executes, in the public interest, the securities laws of the United States." Pet. App. B21. Thus, the court continued, "[t]here is nothing inherent in the SEC's dual role that suggests that the SEC's various functions are mutually exclusive. By giving the SEC a broad range of responsibilities and enforce-

ment rights, Congress indicates just the contrary. The diverse statutory provisions authorizing SEC action confirm this conclusion." *Ibid.* See 15 U.S.C. 78o(b)(4) and (6), 80b-3(e) and (f). Accordingly, the court below correctly held that "the Maloney Act's limitations of the SEC's review over NASD disciplinary action do not constitute limitations of the SEC's other enforcement rights and obligations." Pet. App. B22; see also *id.* at B14 (noting that "the SEC has repeatedly interpreted the Maloney Act not to inhibit its independent inquiry into improper practices," and citing cases).

Petitioner also errs in suggesting (Pet. 4-5) that the SEC may not regulate in areas subject to enforcement by the NASD. Congress expressly granted the NASD and the SEC overlapping responsibility to bring disciplinary proceedings against securities professionals for violations of the Exchange Act or rules and regulations thereunder, see 15 U.S.C. 78o-3(b)(4), (6) and (7). Moreover, Congress has granted the SEC a broader range of remedies than are available to the NASD. Thus, while "the NASD's greatest sanction is merely to expel a member, revoke his registration, and bar him from association with NASD members," Pet. App. B14, the SEC may ban a person from registering as, or from associating with any, broker-dealer *or* investment adviser, and may issue a cease and desist order, 15 U.S.C. 78u-3. Petitioner points to nothing in the Maloney Act that suggests that a person is immune from those statutory remedies and penalties if he is first subject to disciplinary sanc-

tions imposed by a self-regulatory national securities association.[3]

2. Petitioner also contends (Pet. 8-11) that the court of appeals improperly rejected his defense of claim preclusion, or res judicata, under which "a judgment on the merits in a prior suit bars a second suit involving the same parties or their privies based on the same cause of action." *Parklane Hosiery Co.* v. *Shore*, 439 U.S. 322, 326 n.5 (1979). Accord *Richards* v. *Jefferson County*, 116 S. Ct. 1761, 1764-1765 (1996); *Martin* v. *Wilks*, 490 U.S. 755, 761 (1989). The court of appeals properly rejected that defense on the grounds that the SEC was neither a party to, nor in privity with a party to, the NASD proceeding, and that the two proceedings are not based on the same cause of action. Pet. App. B12-B19.

a. The court of appeals concluded that the SEC was not a party, or in privity with a party, to the NASD proceeding. Pet. App. B16-B19. In arguing to the contrary, petitioner contends that the NASD and the SEC are "two wings of a single federal agency," Pet. 11, and that there is privity between the NASD and the SEC because their officers represent "the same government," Pet. 8 (quoting *Sunshine An-*

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[3] Petitioner also relies (Pet. 4-5) on suggestions in the legislative history of the Maloney Act that authorizing the NASD to bring proceedings would reduce the number of enforcement proceedings initiated by the SEC. Nothing in that history, however, indicates that Congress intended to preclude the SEC from bringing its own proceedings when it believes that further sanctions are appropriate. See also Pet. App. B21 (noting that "as a matter of policy, [the SEC] does not impose sanctions on NASD members when it determines that NASD sanctions are sufficient[,] and * * * it initiates action on its own only when doing so is necessary in the 'public interest'").

thracite Coal Co. v. *Adkins*, 310 U.S. 381, 402 (1940)). That is not correct.

The NASD is a private corporation, not a government agency. Pet. App. B13, B20. Moreover, while the NASD is subject to extensive oversight by the SEC, that oversight does not transform it into the SEC.[4] As the court of appeals correctly explained, "[t]he SEC prosecutor, *i.e.* its enforcement division, was never a party to the NASD proceeding and it would not, in the ordinary course, have been a party even if the SEC as adjudicator had reviewed the NASD order." *Id.* at B17; see also *ibid.* ("NASD's interest in prosecuting a disciplinary action does not represent the same legal right that the SEC has in reviewing it.").

b. Petitioner also argues that the NASD and SEC proceedings involve the identical cause of action because the SEC has acknowledged that the two proceedings were "based on substantially the same allegations." See Pet. 10 (quoting Pet. App. A23 n.36). Even assuming that the SEC could be considered the

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[4] Petitioner cites no decision holding that the NASD should be treated as the SEC for all purposes, or even for purposes of applying preclusion principles. The decisions petitioner relies upon (Pet. 5) involve whether the NASD or its officials are immune from suit, *Austin Mun. Sec., Inc.* v. *National Ass'n of Sec. Dealers, Inc.*, 757 F.2d 676, 689-692 (5th Cir. 1985); *Mandelbaum* v. *New York Mercantile Exch.*, 894 F. Supp. 676, 678-682 (S.D.N.Y. 1995); *Bruan, Gordon & Co.* v. *Hellmers*, 502 F. Supp. 897, 902-903 (S.D.N.Y. 1980); whether such officials are akin to federal officials for purpose of jurisdiction, *Bruan, Gordon*, 502 F. Supp. at 901-902; or whether a plaintiff may claim that NASD rules tortiously interfered with private contracts, *Harwell* v. *Growth Programs, Inc.*, 315 F. Supp. 1184, 1191 (W.D. Tex. 1970), rev'd, 451 F.2d 240 (5th Cir. 1971), cert. denied, 409 U.S. 876 (1972).

"plaintiff" in the NASD's disciplinary proceeding, however, it is well established "that claim preclusion generally does not apply where '[t]he plaintiff was unable to rely on a certain theory of the case or to seek a certain remedy because of the limitations on the subject matter jurisdiction of the courts.'" *Marrese* v. *American Academy of Orthopaedic Surgeons*, 470 U.S. 373, 382 (1985) (quoting Restatement (Second) of Judgments § 26(1)(c) (1982)); see also 18 C. Wright, A. Miller, and E. Cooper, *Federal Practice and Procedure* § 4412, at 94 (1981) ("Matters that can be advanced only before an administrative agency ordinarily do not form part of a single claim with matters that can be advanced only before another agency or a court.").

As the court of appeals explained, the SEC proceeding involved claims and forms of relief that could not have been advanced by the NASD. Pet. App. B16. For example, the SEC charged petitioner with aiding and abetting violations of antifraud provisions of the Investment Advisers Act of 1940, 15 U.S.C. 80b-6(1) and 6(2), a matter outside the NASD's jurisdiction. See 15 U.S.C. 78o-3(b)(7) (defining violations for which members may be disciplined). The SEC also imposed sanctions on petitioner, such as a suspension from association with any investment adviser, and a cease and desist order, that were not available to the NASD. Pet. App. B15-B16. It would be inappropriate to preclude the SEC from carrying out its broad statutory enforcement responsibilities simply because the NASD, acting under different and limited statutory authority, first brought a disciplinary proceeding based on the same conduct. Accordingly, the

court of appeals properly held that the SEC's administrative proceeding was not barred by principles of res judicata.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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